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IN THE

Supreme Court of the United States

VERIZON COMMUNICATIONS INC.,

Petitioner,

v.

LAW OFFICES OF CURTIS V. TRINKO, LLP,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR COVAD COMMUNICATIONS COMPANY, INC. AS *AMICUS CURIAE* IN SUPPORT OF RESPONDENT

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INTEREST OF AMICUS

Amicus Covad Communications Company ("Covad") is a competitive local exchange carrier ("CLEC"). Covad is the largest independent provider of digital subscriber line ("DSL") service, a low-cost means of providing high-bandwidth internet access to businesses and consumers. Covad provides DSL service to the public through a combination of its own extensive network facilities and discreet, nonduplicable elements of the monopoly local telephone networks of incumbent local exchange carriers ("ILECs") such as Verizon.[1]

Covad has experienced first hand ILEC anticompetitive conduct of the type that is the subject of this action. Covad has been and continues to be severely harmed by that conduct while other DSL providers, and numerous other CLECs, have been driven out of business altogether.

Covad has two pending antitrust actions against ILECs for this very conduct now before the Courts of Appeals for the Eleventh Circuit (against BellSouth) and the District of Columbia Circuit (against Verizon). In both actions, the ILECs moved to dismiss at the pleading stage and Covad appealed. The District of Columbia Circuit has stayed Covad's appeal pending a decision in this case. *Covad Communications Co. v. Bell Atlantic Corp.*, No. 02-7057. The Eleventh Circuit reinstated Covad's claims against BellSouth. *Covad Communications Co. v. BellSouth Corp.*, 299 F.3d 1272, *reh'g denied* 314 F.3d 1282 (11th Cir. 2002). The case is stayed while BellSouth's Petition for a writ of certiorari to the Eleventh Circuit is pending before this Court. *BellSouth Corp. v. Covad Communications Co.*, No. 02-1423 (petition filed Mar. 20, 2003).

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1. Pursuant to Supreme Court Rule 37.6, Covad states that no counsel for any party authored this brief in whole or in part, and that no person or entity, other than Covad and its counsel, contributed monetarily to the preparation or submission of this brief.

The parties have consented to the filing of all amicus briefs. Pursuant to Supreme Court Rule 37.3, letters evidencing these consents have been filed with the Clerk.

SUMMARY OF THE ARGUMENT

More than seven years have passed since Congress enacted the Telecommunications Act of 1996, 47 U.S.C. §§ 151, *et seq.* (the "1996 Act"), which was designed to bring true competition to local telecommunications markets. But as the United States observes, "[s]ince then, the incumbent local exchange carriers (ILECs), such as the Bell Companies that inherited AT&T's local telephone franchises, have remained dominant." Brief for the United States and the Federal Trade Commission as Amici Curiae Supporting Petitioner ("US/FTC Br."), 2. Competition has not materialized because the ILECs have manipulated the competitive and regulatory landscapes to extend their long-sanctioned, rate-payer funded local telephone monopolies into monopolies over other, emerging markets, including the markets for Internet access, in which Covad competes. The ILECs' persistent misconduct has devastated the competitive landscape. Many competitors have been forced out of business altogether and others, such as Covad, have been grievously injured. The ILECs' determination to exclude competition, and their success in doing so, despite the provisions of the 1996 Act, make clear the need for antitrust enforcement to bring an end to their exclusionary practices. Without such enforcement, competition will *never* develop.

1. The ILECs are engaged in a pattern of conduct that has been designed to and does devastate competition. They routinely proffer outright denials of access to their networks, engage in effective denials through the mechanism of conscious, unreasonable delays even when ostensibly deigning to provide access, and take countless steps to raise their rivals' costs so as to drive out competition (including by implementation of an anticompetitive price squeeze with regard to DSL). Through this course of conduct they have succeeded both in destroying most market entrants, and also in consolidating and expanding their own monopoly power.

2. The ILEC conduct about which Respondent and Covad complain is not novel territory unrecognized by the antitrust laws. Rather, traditional antitrust doctrines developed over

many decades preclude the precise type of misconduct in which the ILECs are engaged, precisely because it harms competition.

One need venture no further than the history of the telecommunications industry itself to reject the ILECs' notion that their conduct is beyond the reach of the antitrust laws. Their duty to provide reasonable access to their monopoly networks was expressly codified by the 1996 Act, but long predated it under the antitrust laws. AT&T's divestiture resulted directly from anticompetitive tactics virtually indistinguishable from those now perpetrated by its corporate progeny. Those practices have been recognized as unlawful under a number of traditional antitrust doctrines, long before the 1996 Act. The ILECs' attacks on antitrust doctrines such as essential facilities and monopoly leveraging simply ignore this Court's teachings in a misguided focus on labels. Whatever label is applied, this Court has long and consistently held that a monopolist violates Section 2 of the Sherman Act when it extends its monopoly over one market into monopoly power over another market. That is precisely what the ILECs stand accused of doing.

3. Verizon and its amici propose a new and unfounded test for Section 2 liability involving refusals to deal among competitors. They propose importing a quasi-predatory pricing standard, by which conduct is only unlawful if a monopolist has forsaken otherwise profitable sales to drive away competition. The Court has never adopted such a standard, and should not do so. Conduct need not involve a sacrifice of profits to be exclusionary. Rather, any conduct that excludes competition on a basis other than efficiency is exclusionary when engaged in by a monopolist. For example, monopolists in control of a nonduplicable network are uniquely positioned to exclude competition without ever sacrificing profits, merely by raising their rivals' costs.

Even if Section 2 liability depended on a showing that a monopolist has forsaken profits, the ILECs would be liable here and in the cases Covad has brought. Covad, like the CLEC in this case, does not seek to take any element of the ILECs'

networks for free. Rather, the 1996 Act incorporates a pricing structure that is, by law, profitable. Thus, each time the ILECs refuse to deal with CLECs such as Covad, they fail to utilize unused capacity on their networks. They thereby turn away profits and fail even the ILECs' imagined test for Section 2 liability.

ARGUMENT

I. The ILECs Routinely Engage In Exclusionary Conduct That Harms Competition

The antitrust laws and the 1996 Act have the same express goal - promoting competition. Section 2 prohibits exclusionary conduct that harms competition: the use of monopoly power "to foreclose competition, gain a competitive advantage, or destroy a competitor." *Eastman Kodak Co. v. Image Technical Services, Inc.*, 504 U.S. 451, 482-83 (1992) (*quoting United States v. Griffith*, 334 U.S. 100, 107 (1948)). Verizon turns the law and the facts upside down, claiming Section 2 should ignore whether "competitors remain viable" because competition itself "harms all rivals" and can "lead to a monopoly market." Brief for Petitioner ("Verizon Br."), 25. Section 2, however, evaluates both the means employed and the effects on competition. What a firm may acquire by means of *fair* competition is quite distinct from what a firm may do while wielding pre-existing monopoly power.

Verizon and its fellow ILECs have not engaged in fair competition. Their success is not due to "innovation or economies of scale or scope" as Verizon contends, Verizon Br. 25, but to their misuse of their historical monopoly of the local telephone network - which competitors must access to compete. They use their control over the local network to starve out their rivals and gain long-term competitive advantages. Verizon and its ILEC amici attempt to dismiss protests about their misconduct as mere quibbles about the particulars of contract performance. *See, e.g.*, Brief Amicus Curiae of BellSouth Corporation, SBC Communications, Inc., and Qwest Communications International, Inc. in Support of Petitioner ("BellSouth Br."), 2 (claim "based on routine performance disputes between contracting parties"). Their misconduct goes

far beyond mere technical breaches of contracts. It was and is intentional, so pervasive as to become institutionalized, and, unfortunately, highly successful. The ILECs have not only harmed competition, they have crippled it and, if left unchecked, fully intend to eliminate it.

A. ILEC Misconduct Affects Far More Than Local Phone Service Resellers

Respondent presents a compelling case that Verizon's exclusionary practices have harmed competition for the provision of basic local telephone service. But Covad addresses an even more serious problem. The ILECs have used, and continue to use, their control over the local telephone network facilities not merely to dominate the local telephone service market, but to gain and maintain monopoly power over entirely distinct markets. Covad participates in such markets, for local Internet access, and has experienced firsthand the ILECs' unlawful practices.[2] Verizon and the other ILECs are engaged in a pattern of conduct designed to exclude Covad and other competitors from competing with the ILECs for customers who want to connect to the Internet.

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2. The Second Circuit chose not to address the potential antitrust claims of CLECs in the context of the 1996 Act. *See Law Offices of Curtis V. Trinko v. Bell Atlantic Corp.*, 305 F.3d 89, 113 n.19 (2d Cir. 2002). However, to the extent the Court reaches the issue in this case, it is clear Covad, itself injured and participating in a market where the ILECs have successfully driven out all other non-ILEC competitors (*see* pp. 15-16 *post*), if anything has a substantially stronger claim of antitrust injury than even Respondent. *See, e.g., American Ad Mgmt., Inc. v. General Tel. Co. of Cal.*, 190 F.3d 1051, 1058 (9th Cir. 1999) ("[I]t is not the status as a consumer or competitor that confers antitrust standing, but the relationship between the defendant's alleged unlawful conduct and the resulting harm to the plaintiff."); *Indeck Energy Services, Inc. v. Consumers Energy Co.*, 250 F.3d 972, 977 (6th Cir. 2000) ("Although antitrust actions may, of course, be initiated by marketplace competitors, those actors in the economic forum must at least allege that exclusion of the competitor from the marketplace results in the elimination of a superior product or a lower-cost alternative"). Here, Covad has a direct relationship with the ILECs and its alleged injury results directly from the ILECs' exclusionary conduct. Whatever derivative injury consumers incur by reason of the harm to Covad may be worthy of redress, but certainly no more so than Covad's direct injuries.

Covad is a facilities-based CLEC. It independently owns, operates and maintains its own telecommunications transmission and related facilities instead of simply reselling the ILECs' telecommunications services. Verizon relies heavily on the inaccurate notion that its competitors simply resell its services. *See, e.g.*, Verizon Br. 3 (rivals "resell [ILECs'] services as mere marketers and middlemen"), 26 (disputing obligation to sell to "mere resellers"), 30 ("the rival simply resells the incumbent's service"); Brief of United Parcel Service, Inc., Honeywell International Inc., Visa U.S.A., Inc., and Eastman Kodak Company as *Amici Curiae* in Support of Petitioner ("UPS/Kodak Br."), 21 (rivals "resell the product or service at retail in direct competition with the firm"). Verizon is wrong. Facilities-based CLECs like Covad are not "mere resellers" of ILEC services. Covad undertook the massive investment to develop, build and support its own network. Thus, when Verizon and other ILECs refused to deal with Covad, they were not merely maintaining their existing monopoly but attempting to extend it into markets where access to the local telephone network was essential to competition. That conduct violates the antitrust laws, and always has.

B. Covad And The Deployment Of DSL Technology

The story of the ILECs' anticompetitive campaign against Covad and other DSL providers begins with the classic symptom of monopolistic complacency: suppression of innovation. Actions that "suppress alternative technology undeniably quash market competition which hurts consumers in a manner prohibited by the antitrust laws." *Int'l Bhd. of Teamsters v. Phillip Morris, Inc.*, 34 F. Supp. 2d 656, 663 (N.D. Ill. 1998), *aff'd*, 196 F.3d 818 (7th Cir. 1999); *see also United States v. Microsoft*, 253 F.3d 34, 76-78 (D.C. Cir.) (en banc), *cert. denied*, 534 U.S. 952 (2001) (Microsoft violated the Sherman Act by, among other things, suppressing Java technology development by competitors).

1. ILECs Suppressed DSL Technology

ILECs had DSL technology and the capability to deploy it for years before the 1996 Act but suppressed its development and deployment and withheld it altogether from the

consuming public to gain further monopoly profits from more expensive, less efficient, internet access services.[3]

At the time, due to the rapid acceleration of Internet use, the Internet access market was ripe for an affordable high-speed alternative technology. To fill that void, Covad introduced DSL, a "dedicated" local communications service that does not travel on the public, switched telephone network. Unlike switched offerings, dedicated services operate directly between two set points, provide high speed digital connections (as much as 50 times faster than the standard 28.8k modem used for dial-up internet access), and are continually connected. Thus, DSL customers get fast service, do not need to dial up every time they want to utilize the service, and they pay a flat, monthly fee, regardless of the amount of time they actually spend using the service. DSL technology is also affordable, because it operates over existing copper phone lines – the same ones ILECs use to provide voice telephone service and much slower or less cost-effective internet access services – obviating special trenching or cable installation that, until then, was necessary to get high-speed dedicated connectivity.[4]

Although DSL technology had been available for a number of years, Verizon and other ILECs suppressed it because they did not want to reduce their revenues from more profitable services. Specifically, ILECs offered: 1) POTS ("plain old telephone service"), the basic analog local telecommunications service used for voice calls and for dial-up connections to the Internet via modems, 2) ISDN ("Integrated Services Digital Network"), a digital dial-up telecommunications service that relies on the same telephone lines and infrastructure that is

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3. Complaint, *Covad Comm. Co. v. BellSouth Corp.*, No. 1:00-CV-3414, ¶ 15 (N.D. Ga. Dec. 22, 2000) ("BellSouth Compl."); Second Amended Complaint, *Covad Comm. Company v. Bell Atlantic Corp.*, No. 1:99-CV-01046, ¶ 45 (D.D.C. Aug. 10, 2000) ("Verizon Compl."). We expect the ILECs may dispute some of the facts asserted here. But because Covad's cases against ILECs such as Verizon and BellSouth are challenged, like Respondent's claims, at the pleading stage, it is the complaints' allegations, and not the ILECs' denials, that matter.

4. *See* BellSouth Compl., ¶¶ 7, 14, 18-21; Verizon Compl., ¶¶ 46-48.

used to provide POTS, and for which customers pay per minute charges; and 3) T-1 and Frame Relay, dedicated high-speed services run on (expensive) lines specially-installed for the individual user, usually a large business.[5]

2. The Response to the Threat Posed by Covad

Covad and other CLECs formed to take advantage of the DSL technology the ILECs had suppressed.[6] When that competitive threat emerged, however, the ILECs immediately raised significant barriers to impede competitive entry. In so doing, the ILECs delayed the initial commercial offering of DSL to the public (and competitive entry into the market) by more than a year, made impossible the widespread dissemination of DSL by CLECs, and guaranteed for themselves continued monopoly profits from other services.[7] More importantly, the delay gave the ILECs the time necessary to develop and deploy their own DSL offerings without fear of losing any competitive advantage to earlier entrants.[8] In the process, ILECs enacted arbitrary policies applicable only to CLECs that further raised CLEC costs for deploying DSL. This was possible solely because the ILECs controlled the key component to DSL delivery that competitors could not duplicate: the ubiquitous local telephone network.

Covad and other DSL CLECs need access to the local telephone network to provide DSL service. In particular, Covad must "collocate" – physically place equipment in ILEC facilities

5. *See* BellSouth Compl., ¶¶ 15, 17-22; Verizon Compl., ¶¶ 55-59.

6. *See* Verizon Compl., ¶¶ 45, 69; BellSouth Compl., ¶ 14.

7. *See* Verizon Compl., ¶¶ 69-70, 97; BellSouth Compl., ¶¶ 1, 45-46, 57.

8. All technology-focused industries place a great premium on being first to market. *See* Verizon Compl., ¶ 67. Once a system is up and running, it is more difficult for a competitor to get a potential customer to undergo the trouble and inconvenience of switching to another provider. *See id.* Therefore, "even minor delays" in interconnecting with an ILEC "can represent a serious and damaging business impediment to competitive market entrants." Second Report and Order, *In the Matter of Implementation of the Telecommunications Act of 1996*, 13 F.C.C.R. 17,018, ¶ 3 (July 14, 1998).

such as "central offices"[9] ("COs") – to connect to the existing telephone network.[10] It must also have access to the copper telephone wires (called "local loops") that connect businesses and residents to COs, and "transport" facilities, which are broadband transmission pipes that connect various COs to one another.[11]

C. The ILECs' Campaign To Exclude Competition

At every turn, ILECs have taken advantage of their control over the local telephone network to exclude Covad and other Internet access competitors – at first, by outright denials and subsequently, by imposition of unreasonable and expensive requirements and conditions, thereby raising CLEC costs. The ILECs, however, do not impose similar requirements, expenses, or delays on their own retail DSL operations. Instead, they allocate costs in such a way as to price their DSL offerings too low for rivals to match and still cover the high start-up costs the ILECs impose on rival operations.

1. Outright Denials of Collocation

The ILECs begin their exclusion of facilities-based CLECs such as Covad by simply shutting the gates. They routinely deny Covad and other CLECs collocation in numerous COs within their local service territories, unilaterally – and falsely – declaring that no space is available.[12] Because each collocation denial effectively prohibits Covad and other CLECs from serving that CO's

9. Central offices are the facilities where all of the residential and business telephone lines for a given geographic area come together and where the ILECs' telecommunications equipment (such as switches) is located. *See* Verizon Compl., ¶¶ 61-62; BellSouth Compl., ¶ 24. Each state has several hundred COs and none overlap in geography or customers. *See id.* California, for example, has more than 600. *See id.*

10. *See* Verizon Compl., ¶¶ 71, 91-92; BellSouth Compl., ¶ 31.

11. *See* Verizon Compl., ¶¶ 5, 63-64; BellSouth Compl., ¶¶ 25-44.

12. Physical collocation makes little demand on space. Covad's equipment, for example, typically occupies between two and four bays in the CO. Each bay of equipment is approximately seven feet high and two feet wide. *See* Verizon Compl., ¶ 93.

market, the ILECs have controlled whether, when and in which markets CLECs can enter and deploy DSL in competition with the slower or more expensive ILEC services and, later, the ILECs' own DSL offering.[13]

For example, Covad requested collocation in a CO in the District of Columbia metropolitan area. Bell Atlantic ("Verizon")[14] denied collocation, representing to both Covad and the state commission that the CO was a two-story building with very little unused, conditioned space. In fact, the CO has four floors and plenty of unused space suitable for collocation. In this false manner, Verizon has denied Covad collocation in many critical market COs within its territory, including Arlington, Crystal City, Tyson's Corner, and the Dulles Corridor, in Washington D.C., and Wayne, Conshohocken, Bryn Mawr, King of Prussia, and Landsdale in Pennsylvania. All of these are business centers with large communities of potential Covad small business customers.[15] The experience was the same around the country, no matter the ILEC.[16]

During that one year plus delay when the ILECs claimed there was "no space" for Covad, the ILECs found sufficient space in those COs to install the collocation equipment of their own retail DSL subsidiaries.[17] Indeed, despite the fact that Covad was by far first to market, the ILECs often ended up rolling out their own DSL offering in those disputed CO markets before Covad or any other CLEC.

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13. *See* BellSouth Compl., ¶ 24.

14. Verizon was formed from the merger of GTE Corp. and Bell Atlantic Corp. *See Big is Better*, The Investment Dealer's Digest, November 19, 2001, at 30-35.

15. *See* Verizon Compl., ¶¶ 99-103.

16. For example, Covad's experience in BellSouth's territory was no different. *See* BellSouth Compl., ¶¶ 47-49.

17. *See* Verizon Compl., ¶ 104.

2. Constructive Denials through Unreasonable Conditions

The ILECs' denials of access through control of collocation space have come at a high price for Covad and other CLECs in terms of time, resources, and delayed market entry. But even when ILECs have nominally granted access for collocation, they have taken advantage of every step of the process to create delay and impose additional unreasonable and unwarranted expenses on their rivals, creating an artificial and competitive advantage for their own unburdened DSL products.

a. Unreasonable delay

When ordering collocation, Covad has experienced unreasonable delay at every stage of the collocation request and provisioning process. Covad has often waited upwards of 120 days just to get a price quote for collocation.[18] Once Covad receives the price quote, places the firm order, and pays the required deposit, all that remains is for the ILEC to provision the collocation space. But at that point, the ILECs have again resorted to systematic delay tactics. For example, Covad waited 221 days for space in the Newman, Ga. CO, 228 days for space in Fort Lauderdale, Fla., 247 days in Hollywood, Fla., and in Atlanta, Covad waited more than 120 days for space in 17 of the first 35 COs in which it ordered space.[19] The process, from application to provisioning, took as much as 375 days in Georgia, 244 days in North Carolina, and 323 days in Florida.[20]

b. Anticompetitive build-out requirements

Even where the ILECs agreed to provide Covad with physical collocation, they have hindered Covad's ability to provide competing services by insisting that Covad

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18. *See* BellSouth Compl., ¶¶ 50-53.

19. *See id.*, ¶¶ 54-57.

20. *See id.*, ¶ 57. Other ILECs implemented similar delay tactics in the collocation application and provisioning process. *See* Verizon Compl., ¶ 124.

purchase what is known as a collocation "cage"[21] and inflating the costs of collocation. Since the ILECs actually built the cages, they also set the (often exorbitant) fees for that build. Verizon, for example, required much more than expensive cages; it required CLECs including Covad to build separate corridors, entrances, staircases, and even a bathroom before providing collocation.[22] Indeed, to build out in a single CO, Verizon quoted Covad physical collocation prices as high as $412,226 in Virginia, $368,141 and $252,300 in New Jersey, $115,900 in Pennsylvania, $115,543 in Delaware, and $154,711 in Maryland.[23]

For Covad and other CLECs, the "price-discounted" access Verizon complains of, Verizon Br. 10, 11, has yet to materialize. Verizon not only passed all its costs on to the CLECs attempting to collocate, it charged CLECs as much as *five times* Verizon's costs. In Bethesda, Maryland, for example, Verizon incurred $62,389 in collocation costs for the CO, however, it billed Covad and the other collocating CLECs more than $320,000 in *deposits* (*i.e.* 50% of the collocation price).[24]

c. Arbitrary loop policies

Once Covad has surmounted the first hurdle and collocated in a central office, it then encounters the ILECs' attempts to prevent it from buying and installing local loops. The ILECs have implemented arbitrary loop policies and procedures to limit the type of service CLECs could offer,

21. The collocation cage is a metal cage-like barrier that separates the physical space allotted to the CLECs equipment from the remainder of the CO. *See* Verizon Compl., ¶¶ 73, 105.

22. *See* Verizon Compl., ¶¶ 105-10, 257-59.

23. *See* Verizon Compl., ¶¶ 105-10. In other states, such as Massachusetts and New York, commissions supervised collocation practices more closely, and the average cost for collocation was much lower ($35,000 in Massachusetts and $43,814 in New York). *See id.*, ¶ 111.

24. *See id.*, ¶ 250. Verizon's over-pricing practice was not unique to Bethesda. Verizon demanded, and received, more than $200,000 (for $67,531 in costs) for its Moorestown, N.J. CO, more than $270,000 (for $61,000 in costs) for its Hackensack, N.J. CO, more than $140,000 (for $43,663 in costs) for its Columbia, Md. CO, more than $378,000 (for $154,904 in costs) for its Laurel, Md. CO, and more than $153,000 (for $66,125 in costs) for its Marlton, N.J. CO. *See id.*, ¶¶ 251-56.

hamper CLECs' ability to determine the availability of service to customers at the ordering stage, and add significant delay to the loop (and, thus, overall DSL service) delivery process. Because the ILECs' own retail DSL operations are not subject to these policies, the ILECs created an artificial competitive advantage over CLECs.

BellSouth, for example, implemented a *manual* loop ordering process for CLECs that is, by design, inept and calculated to produce delay, human error and uncertainty at every turn. The ILEC requires, for example, that each order be typed on a (complicated and confusing) request form and submitted manually via facsimile to BellSouth where an employee manually retypes the information into BellSouth's system. BellSouth often rejects (without notice to the CLEC) thousands of orders because the facsimile renders the transmission illegible or it claims the form is improperly filled out.[25] For its own DSL products, by contrast, BellSouth uses an electronic pre-ordering and ordering system which it does not make accessible to CLECs.[26]

Verizon similarly uses loop pre-qualification to impede competition. Verizon initially tied its willingness to provide loop information to its own ability to provide DSL services; when it was not offering DSL service, it simply refused to provide Covad or other CLECs with *any* loop information. Once Verizon deployed its own DSL service, it would only provide loop information for those locations where it provided DSL. In those locations, Verizon would only tell Covad the loop length, omitting other conditions such as load coils or bridged taps that could affect DSL transmission over that loop. In locations where Verizon was not providing DSL, Verizon subsequently claimed that it would only look up the pertinent information manually (even though Verizon had an automated loop information system) and provide it to Covad on a loop-by-loop basis, a time-consuming and ineffective method for

25. *See* BellSouth Compl., ¶¶ 67-68. BellSouth has at times turned off its facsimile machines without notice, and has changed facsimile numbers without notice, later contending that large numbers of orders were never received. *See id.*

26. *See id.*, ¶¶ 70-71.

handling the volume of loop orders Covad placed with Verizon. Under Verizon's system, therefore, Covad – unlike Verizon – could not guarantee its customers in advance what speed service they would get or when.[27]

3. Discrimination Against Rivals

The ILECs also discriminate against CLECs, and in favor of the ILECs' own retail DSL operations by dictating the very technology CLECs can use to provide DSL services. ILECs do this for no technologically sound reason, but rather to gain competitive advantages in, and therefore dominate, the Internet access markets.[28] "[A] parent corporation may favor its subsidiary so long as it does not lead to control of the relevant market." *H&W Indus., Inc. v. Formosa Plastics Corp., U.S.A.*, 687 F. Supp. 271, 276 (N.D. Miss. 1988), *rev'd on other grounds*, 860 F.2d 172 (5th Cir. 1988); *see also M&M Med. Supplies & Serv., Inc. v. Pleasant Valley Hosp., Inc.*, 981 F.2d 160, 166-68 (4th Cir. 1992) (vacating summary judgment in Section 2 action alleging hospital monopolized medical equipment market by marketing only its medical equipment subsidiary's products).

The ILECs have blatantly engaged in discrimination regarding a particularly promising technology for delivering DSL service, known as "line sharing." Line sharing permits a single local loop to carry both basic voice telephone service and DSL service to a customer, simultaneously.[29] A customer receiving DSL service via line sharing, therefore, does not need a second local loop.[30] But instead of permitting Covad and

27. *See* Verizon Compl., ¶¶ 125-130.

28. Relying on a Robinson-Patman Act discussion in a treatise, Verizon suggests a Section 2 action cannot be sustained when the allegation is that a parent company discriminated between its subsidiary and unrelated companies. Verizon Brief 18-19 & n.15. Unlike the Robinson-Patman Act (and Section 1 of the Sherman Act), Section 2 combats both unilateral and concerted actions that cause monopolization. *See Copperweld Corp. v. Independence Tube Corp.*, 467 U.S. 752, 776-77 (1984) ("Any anticompetitive activities of corporations and their wholly owned subsidiaries meriting antitrust remedies may be policed" by Section 2).

29. *See* BellSouth Compl., ¶ 84; Verizon Compl., ¶¶ 180-81.

30. *See, e.g., DSL FAQ: Why is a line sharing install easier?*, Broadband Reports.com, *available at* http://www.dslreports.com/faq/402.

other CLECs to use existing voice lines to provide digital service, Verizon and BellSouth have required Covad to procure a *second* line – that is, a new loop – to offer DSL service. At the same time, their own DSL operations utilize line-sharing.[31]

By forcing CLECs to purchase a second loop to service their customers and manipulating the process of allocating the cost of those local loops, the ILECs achieve an anticompetitive price squeeze. To price their retail DSL service, the ILECs attribute only a negligible portion of the cost of the local loop to DSL and other data services, attributing the overwhelming majority of the cost to the analog voice service they provide on the same line. The ILECs then set the retail prices for their DSL services at or below the price they charge CLECs for the wholesale unbundled loop ILECs require CLECs to purchase to offer DSL. Unable to match the ILEC DSL retail price and make a reasonable return on their investment, CLECs are trapped between the price they must pay as ILEC customers for the loop and the DSL retail price set by ILECs as competitive DSL providers.[32] The ILECs thus extend their monopoly over local loops into control over DSL service as well.

D. ILECs All But Destroyed Competition And Increased Their Monopolies

By means of this intentional pattern of conduct, ILECs successfully eliminated or seriously injured their rival CLECs and expanded the scope and reach of their monopolies. As one commentator aptly described the current situation:

> What's left of Ma Bell's progeny – BellSouth, Qwest, SBC, and Verizon – have maintained their lock on local phone service and driven most of their newfangled rivals to the hills. They've moved successfully into new markets like wireless and broadband Net access.

Jason Krause, *Dawn of the Big Bells*, The Industry Standard, April 20, 2001, *available at* http://www.thestandard.com/article/0,1902,23871,00.html. Indeed, the ILECs'

31. *See* BellSouth Compl., ¶ 85; Verizon Compl., ¶ 181.

32. *See* BellSouth Compl., ¶ 84-86; Verizon Compl., ¶ 179-84.

anticompetitive conduct "effectively dr[ove] every major [DSL] competitor except Covad out" of business. *Id.* All three of the prominent CLECs offering DSL service in direct competition with ILEC internet access offerings - Covad, Rhythms, and Northpoint - were forced into bankruptcy; all but Covad ceased doing business altogether. *See* Todd Wallack, *Covad Knows How To Survive*, S.F. Chron., Feb. 10, 2003, at E1; Todd Wallack, *Covad Makes A Comeback From Bankruptcy*, S.F. Chron., Sept. 6, 2002, at B1; *see also* Stephen P. Pizzo, *Why is Broadband So Narrow?*, Forbes, Inc., Sept. 10, 2001, at 50.

The ILECs reduced not only the ranks of their competitors, but their own ranks, via merger, thereby enhancing their already enormous monopoly power. The 1984 break-up of AT&T resulted in seven Regional Bell Operating Companies ("RBOCs," i.e. ILECs); now, as a result of several recent mergers, there are only *four*: Verizon (the largest), SBC, Ameritech, and Qwest. *See Big is Better, ante.* These four mega-ILECs dominate local telephone network facilities in enormous multi-state regions, and provide DSL and other Internet access services to an overwhelming percentage of the population in those states.

That intense consolidation was permitted only on the premise of the ILECs' ongoing obligations to open their networks to competition under the 1996 Act and further obligations assumed by the merging ILECs to compete with one another. *See* David Rohde, *Bells Are Failing to Compete As They Promised*, Network World, Inc., Mar. 5, 2001, at 1, *available at* http://www.nwfusion.com/news/2001/0305bellcomp.html. None of this promised competition has materialized. *See id.*; *see also* Krause, *Dawn of the Big Bells, ante*. As a result, the ILECs have taken the benefits of the 1996 Act with none of its burdens. The Act guards against this by means of antitrust enforcement.

II. Antitrust Remedies Are Necessary, Proper And Traditional Means To Combat ILECs' Anticompetitive Conduct

Verizon and its amici have mythologized the antitrust laws to create the appearance that access to their state-created, ratepayer-funded local monopoly networks would never be appropriate under the "unadorned antitrust laws." In reality,

many decades of antitrust law, in both regulated and unregulated industries, make clear that no monopolist may engage in the type of exclusionary conduct the ILECs have practiced so relentlessly for the past seven years. The claims against Verizon in this case are nothing new. Rather, they arise from the same conduct - abuse of the unique monopoly power inherent in the local telephone network - that led to the breakup of the old AT&T Bell System twenty years ago.

A. Traditional Sherman Act Section 2 Doctrines Forbid The ILECs' Exclusionary Practices

This Court has long held that there are defined limits on a monopolist's privilege not to deal with its rivals:

> It is true that as a general matter a firm can refuse to deal with its competitors. But such a right is not absolute; it exists only if there are legitimate competitive reasons for the refusal.

Kodak, 504 U.S. at 483 n.32 (1992); *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585, 601 (1985) ("right to refuse to deal with other firms does not mean that the right is unqualified"). As in *Kodak*, the conduct alleged here, which involves "market foreclosure," is "facially anticompetitive and exactly the harm that antitrust laws aim to prevent." 504 U.S. at 478.

Verizon and its amici rely heavily on critiques from various commentators to mask the lack of legal precedent for what their position truly represents: a dramatic change in how the antitrust laws treat exclusionary conduct by vertically integrated monopolists. But the Court has long recognized that the value of such theoretical economic constructs is limited, particularly where, as here, the Court is reviewing the case without benefit of a developed factual record. *See, e.g., Kodak.*, 504 U.S. at 486 ("In the end, of course, Kodak's arguments [about interbrand competition logically disciplining intrabrand market power] may prove to be correct. . . . But we cannot reach these conclusions as a matter of law on a record this sparse"). Covad's claims, like Respondent's, are challenged on the pleadings, not after development of facts through

discovery. At the pleading stage, the claims asserted by Respondent (and those asserted against the ILECs by Covad) state well recognized violations of Section 2 of the Sherman Act.

1. The Unique History of the Regulated Telecommunications Industry Demonstrates the Importance of Antitrust Enforcement

The 1996 Act may indeed have been "something brand new" when it was enacted seven years ago. Verizon Br. 2. But the need to restrain exclusionary abuses by those who control the local telephone network is nothing new. Local telephone monopolists have long been using their control over the nonduplicable local network – a network that literally connects by wire all end users in a given geographic region – to exclude competition in other markets that depend on access to that monopolized local network. Verizon's amici assert that an "ILEC's affirmative duties to share its resources with rivals derive not from antitrust law but from the 1996 Act." BellSouth Br. 8. They ask the Court to ignore the history of the antitrust laws, and in particular the painful history of anticompetitive conduct by local monopolists in the telecommunications industry.

The requirement to provide reasonable access to elements of the local telephone network did not originate with the 1996 Act but existed decades before it. Local telephone monopolists have long been required to provide competitors full access to their local networks, through a process called interconnection. *See In the Matter of Establishment of Policies and Procedures for Consideration of Application to Provide Specialized Common Carrier Services in the Domestic Public Point-to-Point Microwave Radio Service and Proposed Amendments to Parts 21, 43, and 61 of the Commission's Rules*, 29 F.C.C.2d 870, 940, ¶ 157 (1971) ("*Specialized Common Carrier*"). The FCC regulated that interconnection duty and AT&T was famously found to have violated the antitrust laws for failing to comply with it.

Interconnection is not one duty, but a set of duties. It has long included the obligation to lease local loops to competitors, who are entitled to full use of them. *See, e.g., Nat'l Ass'n of Regulatory Util. Comm'rs v. F.C.C.*, 737 F.2d 1095, 1106 (D.C. Cir. 1984); *Bell Tel. Co. of Pa. v. F.C.C.*, 503 F.2d 1250, 1259

(3d Cir. 1974); *MCI Comm. Corp. v. AT&T Co.*, 708 F.2d 1081, 1140 & n.88 (7th Cir. 1983); *Specialized Common Carrier*, 29 F.C.C.2d at 938, 940, ¶¶ 151, 157; *see also MCI*, 708 F.2d at 1133 (finding MCI's request to lease local loops was not a request to abandon facilities). Interconnection also obliged local monopolists to provide physical connection between the local network and competing networks – the same duty embraced under the 1996 Act by collocation. *See United States v. AT&T Co.*, 524 F. Supp. 1336, 1352-53 (D.D.C. 1981) ("*AT&T*") ("Long distance and other intercity lines are essentially useless unless they can be connected to the local switches."). Those duties expressly applied to ensure reasonable access for competitors providing advanced services, such as the DSL service Covad provides. *See California v. F.C.C.*, 39 F.3d 919, 929 (9th Cir. 1994) (recognizing pre-1996 FCC order that "BOCs must provide other enhanced service providers the same interconnections the BOCs use in providing their own services"); *see also In the Matters of Amendment of Sections 64.702 of the Commission's Rules and Regulations*, 2 F.C.C.R. 3072, 3080, ¶ 61 (May 22, 1987) ("carriers must provide efficient nondiscriminatory access to the basic service facilities necessary to support their competitors' enhanced services").

The ILECs' pre-1996 obligations included not just the duty to provide access, but to do so on "just and reasonable terms" that would place competitors on "as nearly as equal plane as may be." *AT&T*, 524 F. Supp. at 1353 (*quoting United States v. Terminal R.R. Ass'n of St. Louis*, 224 U.S. 383, 411 (1912)); *California v. F.C.C.*, 905 F.2d 1217, 1229 (9th Cir. 1990) (noting FCC's *pre-1996* "open-network policy of requiring the BOCs to make the telephone networks as accessible to competitors as they are to the BOCs themselves"). Indeed, AT&T was found liable under the Sherman Act some twenty years ago for forcing interconnections to take place by means of "inappropriate or inefficient equipment or procedures." *MCI*, 708 F.2d at 1150.

Beyond its straight refusals to provide reasonable access to its monopoly local network, AT&T also took advantage of the regulated nature of the industry to impede competition:

> Finally, and most importantly, the filings with the state commissions (as a culmination of the

> negotiations) added additional months of delay before MCI could enter the market. The combined effect of the bad faith negotiations and the filing of the state tariffs may have cost MCI one and a half years of time and revenue while it fought for interconnections, first with AT&T at the bargaining table and later in the FCC and the courts.

MCI, 708 F.2d at 1158.

The same pattern of obstruction and delay has continued under the 1996 Act, as described in detail above. *See* pp. 6-16, *ante*. As this Court has recognized, ILECs have caused competitively meaningful delays through refusals to comply with the 1996 Act:

> A separate rate for an unbundled element is not much good if . . . the incumbents refuse to allow the leased elements to be combined with a competitor's own equipment. And this is just what was happening before the FCC devised its combination rules. Incumbents, according to the FCC's findings, were refusing to give competitors' technicians access to their physical plants to make necessary connections.

Verizon Comm., Inc. v. F.C.C., 535 U.S. 467, 532 (2002). Indeed, just as the old AT&T did, the ILECs are actively using the litigation process to delay whatever administrative enforcement might otherwise apply. Fully seven years after the 1996 Act was enacted, the basic rules under which it will be administered are still yet to be finally resolved. *See, e.g., United States Telecom Ass'n v. F.C.C.*, 290 F.3d 415 (D.C. Cir. 2002) (remanding implementation order to FCC for a *third* round of reconsideration, six years after 1996 Act enacted). That conduct frustrates competition. *See, e.g., Southern Pac. Comm. Co. v. AT&T Co.*, 740 F.2d 980, 1001-02 (D.C. Cir. 1984) (cost and delay inherent in regulatory process "clearly constitute barriers to entry").

The FCC has observed that even minor delays in providing interconnection to local telephone networks "can represent a serious and damaging business impediment to competitive market entrants" such as Covad and AT&T, the CLEC serving

Respondent. Second Report and Order, *In the Matter of Implementation of the Telecommunications Act of 1996*, 13 F.C.C.R. 17,018, ¶ 3 (July 14, 1998). FCC and state administrative agencies simply do not have the power to deter such conduct, nor to compensate its victims. The FCC acknowledges this. FCC Chairman Michael Powell has told Congress that "[g]iven the vast resources of many of the nation's ILECs," the FCC's current fining authority of $1.2 million per offense "is insufficient to punish and deter violations in many instances." Letter from Chairman Powell to House and Senate Appropriations Committees of 5/4/01. Antitrust remedies, including treble damages and attorneys' fees, are necessary to make the ILECs, with their vast resources, obey the law.

2. Monopoly-to-Monopoly Leveraging is Unlawful

Verizon and its amici attempt to present the concept of monopoly leveraging as somehow beyond the realm of the "real" antitrust laws. *See, e.g.*, Verizon Br. 43 (monopoly leveraging theory is "largely discredited"); BellSouth Br. 20 (monopoly leveraging theory "conflicts with established limits on antitrust law"). That argument is impossible. Decades of this Court's decisions have expressly upheld liability for monopoly leveraging. As the Court observed in *Kodak*, it "has held many times that power gained through some natural and legal advantage such as a patent, copyright, or business acumen can give rise to liability if 'a seller exploits his dominant position in one market to expand his empire into the next." *Kodak*, 504 U.S. at 479-80 n.29 (citing cases). That is a point on which the *Kodak* majority and dissent agreed. 504 U.S. at 498 ("The Court correctly observes that the antitrust laws do not permit even a *natural* monopolist to project its monopoly power into another market") (Scalia, J., dissenting) (emphasis in original).[33]

There can be no question, at this point, that monopoly leveraging is a well-established Section 2 violation. *See, e.g.*,

33. *See also* 504 U.S. at 476 n.23 ("A firm can exact leverage whenever other equipment is not a ready substitute. F. Scherer & D. Ross, *Industrial Market Structure and Economic Performance* 16-17 (3d ed. 1990)"). There is no substitute, ready or otherwise, for critical elements of the ILECs' local telephone network, such as local loops.

United States v. Griffith, 334 U.S. 100, 108 (1948) (monopoly power cannot be used "to beget monopoly"), *overruled on other grounds sub nom. Copperweld*, 467 U.S. at 764 n.8; *United States v. Paramount Pictures*, 334 U.S. 131, 174 (1948). And the attempted extension of even a lawful monopoly is improper "whatever the nature of the device by which" the monopolist attempts to extend its monopoly. *Leitch Mfg. Co. v Barber Co.*, 302 U.S. 458, 463 (1938). Even those ingenious enough to develop a lawfully patented product cannot seek to leverage or extend their monopolies. *Id.* As an historically state-supported and ratepayer-funded monopoly, Verizon has, if possible, even less justification for extending its monopoly power into other markets.

In reality, the ILECs are merely using perceived infirmities in the Second Circuit Court of Appeals' particular formulation of the monopoly leveraging test to eliminate leveraging liability altogether. There is no basis to do so. Whether the Court adopts the Second Circuit's view that gaining a "competitive advantage" in the secondary market suffices, or the more stringent view requiring at least a dangerous probability of obtaining a monopoly in the secondary market, the ILECs fail the test. They have "exploited [their] dominant position" over the local telephone network to gain monopolies, not merely competitive advantage, in a number of additional markets – including, in the case of Covad, the market for Internet access. *See* pp. 15-16, *ante*. Whatever leveraging standard the Court applies, the ILECs' conduct violates the antitrust boundaries this Court long ago established.

3. The Essential Facilities Doctrine Properly Applies to the ILECs' Attempts to Use Their Local Network Monopolies to Control Secondary Markets

Verizon and its amici criticize the essential facilities doctrine at length, pointing out that this Court has never "recognized" the doctrine. *See, e.g.*, Verizon Br. 40; US/FTC Br. 21. But they cannot dispute that all thirteen Courts of Appeal recognize the doctrine, and agree as to its elements.[34]

34. *See, e.g., Hecht v. Pro-Football, Inc.*, 570 F.2d 982, 992-93 (D.C. Cir. 1977), *cert. denied*, 436 U.S. 956 (1978); *Interface Group, Inc. v. Mass. Port Auth.*, (Cont'd)

And so did the United States in its brief in support of Verizon's petition for a writ of certiorari in this matter. The United States described the principle behind "the leading case," the Seventh Circuit's decision in *MCI*, 708 F.2d at 1132-33 as follows: "a monopolist may be required to assist rivals by sharing a facility if the monopolist can 'extend monopoly power from one stage of production to another.'" Brief For The United States And The Federal Trade Commission As Amici Curiae, *Verizon Comm., Inc. v. Law Offices of Curtis V. Trinko*, On Petition for a Writ of Certiorari, No. 02-682 (filed Dec. 2002) at 12 (*quoting MCI*, 708 F.2d at 1132-33).[35] In other words, the essential facilities doctrine as exemplified by *MCI* merely addresses one situation where an unchecked monopolist would otherwise extend its monopoly into a secondary market – conduct the "Court has held many times" is unlawful. *Kodak*, 504 U.S. at 479-80 n.29.

a. Essential facilities claims involve extension of a monopoly into a second market

The essential facilities claim asserted against ILECs by Covad, even more so than the claim asserted by Trinko, fits

(Cont'd)
816 F.2d 9, 12 (1st Cir. 1987); *Delaware & Hudson Ry. Co. v. Consol. Rail Corp.*, 902 F.2d 174, 179-80 (2d Cir. 1990), *cert. denied*, 500 U.S. 928 (1991); *Ideal Dairy Farms, Inc. v. John Labatt, Ltd.*, 90 F.3d 737, 748 (3d Cir. 1996); *Advanced Health-Care Serv., Inc. v. Radford Cmty. Hosp.*, 910 F.2d 139, 150 (4th Cir. 1990); *Mid-Texas Comm. Sys., Inc. v. AT&T Co.*, 615 F.2d 1372, 1387 n.12 (5th Cir. 1980); *Directory Sales Mgmt. Corp. v. Ohio Bell Tel. Co.*, 833 F.2d 606, 612 (6th Cir. 1987); *MCI Comm. Corp. v. AT&T Co.*, 708 F.2d 1081, 1132-33 (7th Cir. 1983); *City of Malden v. Union Elec. Co.*, 887 F.2d 157, 160 (8th Cir. 1989); *City of Vernon v. S. Cal. Edison Co.*, 955 F.2d 1361, 1366-67 (9th Cir. 1992), *cert. denied*, 506 U.S. 908 (1992); *Aspen Highlands Skiing Corp. v. Aspen Skiing Co.*, 738 F.2d 1509, 1520 (10th Cir. 1984), *aff'd on other grounds*, 472 U.S. 585 (1985); *Covad Comm. Co. v. BellSouth Corp.*, 299 F.3d 1272, 1285-88 (11th Cir. 2002), *reh'g denied*, 314 F.3d 1282; *Intergraph Corp. v. Intel Corp.*, 195 F.3d 1346, 1356-57 (Fed. Cir. 1999).

35. Verizon mistakenly asserts that all CLEC claims seek affirmative "assistance" and to force ILECs to "share" their resources. *See, e.g.*, Verizon Br. 11, 27. That is not what Covad seeks. Rather, the ILECs are refusing to lease to Covad elements of their networks that by definition they are not otherwise using, and from which they are not otherwise deriving the income Covad would provide. *See* pp. 26-30, *post*.

perfectly the *MCI* essential facilities test. *MCI* distinguished between two sets of demands for network access by MCI. The Seventh Circuit found MCI stated an essential facilities claim when it sought access to elements of AT&T's monopoly local telephone network that could not reasonably be duplicated, to use those elements to provide a separate and distinct product, long distance service. *MCI*, 708 F.2d at 1132-33. By contrast, the Seventh Circuit found MCI had not proved an essential facilities claim when it sought access to elements of AT&T's long distance network, in part because MCI had not proved the elements it sought to lease were essential (MCI having shown the ability to duplicate them), *id.* at 1147-48, and, given the elements were not essential, MCI could not claim a right to unfettered access to AT&T's entire network merely to provide the same service AT&T was providing. *Id.* at 1149. Verizon has focused on the latter component of the Seventh Circuit's analysis in isolation, to argue that there can be no essential facilities claim when the competitor merely provides the same service as the incumbent whose facilities it seeks to share. Verizon Br. 42. But that is not what *MCI* held, nor would it be a coherent result; if a plaintiff meets the four well-established elements of the essential facilities doctrine, there is no reason to import a new unspoken element that the competitor must participate at a different level of the market than the monopolist.

In any event, even if the essential facilities doctrine were somehow inapplicable to those who resell a monopolist's products in the same market, that would not justify the ILECs' plea to do away with the essential facilities doctrine altogether. It is true that some CLECs merely resell local service they buy from ILECs at wholesale. But many other CLECs, including Covad, use interconnection with and elements of the monopoly local telephone networks to provide competition to the ILECs in markets other than the market for local telephone service. This Court's long-standing Section 2 precedents – whether labeled under the essential facilities doctrine or not – confirm that it is unlawful to wield monopoly power where doing so extends that monopoly power into other markets. *See* pp. 26-30, *post*.

b. Essential facilities claims are especially important in "natural" monopoly markets

Even Verizon's amici concede that an essential facilities approach to refusals to deal is most necessary where the monopolist controls a "natural monopoly." *See* UPS/Kodak Brief 25. Academic commentators have agreed. *See, e.g.*, Phillip E. Areeda, *Essential Facilities: An Epithet in Need of Limiting Principles*, 58 Antitrust L.J. 841, 853 n.21 (1990) (*MCI* "is probably correct [in holding] a monopolist must, when feasible, make its essential facility available to a competitor who is unable to duplicate it."); Herbert Hovenkamp, *Federal Antitrust Policy: The Law of Competition and Its Practice* § 7.7a, 274 (2d ed. 1994) (courts have regularly found to be essential "structures, plants or other valuable productive assets that were created as part of a regulatory regime, whether or not they are properly natural monopolies").

The local telephone network has long been recognized as a paradigm of a "natural" monopoly. *See AT&T Corp. v. Iowa Utils. Bd.*, 525 U.S. 366, 371 (1999) ("States typically granted [the ILECs] an exclusive franchise in each local service area"). As this Court has found, because each local telephone network involves a set of literally many millions of telephone wires connecting each home and business in the region, duplication of that network is impracticable in the extreme. *See Verizon*, 535 U.S. at 490 ("It is easy to see why a company that owns a local exchange . . . would have an almost insurmountable competitive advantage not only in routing calls within the exchange, but, through its control of this local market, in the markets for terminal equipment and long-distance calling as well.").

The courts have consistently found – long before the 1996 Act – that this "natural" monopoly power carries with it an obligation that the local telephone monopolists provide reasonable access to those local network facilities. *MCI*, 708 F.2d at 1133, 1138, 1140-41; *AT&T*, 524 F. Supp. at 1353 ("clear that the local facilities controlled by Bell are 'essential facilities' within the meaning of these decisions"); *Southern Pac. Comm.*, 740 F.2d at 1008 (finding "the Bell operating companies' local distribution facilities are 'essential facilities'" and that the

antitrust laws "prohibit AT&T from unreasonably and discriminatorily restricting access to these essential facilities"); *see also* Phillip E. Areeda & Herbert Hovenkamp, 3A *Antitrust Law* 2d ¶ 772, 175 (2002) ("whether or not local 'hard-wired' telephone service is best delivered by a monopoly, it would be unwise to allow that monopoly to obstruct free competition in long distance services or telephone instruments, where competition is clearly possible").

B. Even Under The ILECs' Unfounded View Of Exclusionary Conduct, Their Conduct Is Still Exclusionary

Verizon and its amici argue for a special, heightened pleading standard for Section 2 refusal to deal claims against vertically integrated monopolists. That position is at odds with their repeated assertions that there are no subcategories of Section 2 offenses – *i.e.*, essential facilities does not exist as an independent claim; monopoly leveraging does not exist, and so on. All Section 2 claims, however labeled, have just two necessary elements: "(1) the possession of monopoly power in the relevant market and (2) the willful acquisition or maintenance of that power." *Kodak*, 504 U.S. at 481 (*quoting United States v. Grinnell Corp.*, 384 U.S. 563, 570-71 (1966)). The conduct the ILECs are alleged to have engaged in more than satisfies that pleading test, the only one this Court has ever said applies to refusal to deal claims. Verizon's proposed test would immunize conduct recognized by established antitrust principles as anticompetitive. In any event, even if the Court adopted the new "predatory pricing" standard Verizon urges, Verizon would still fail the test because it routinely foregoes profits when it refuses to deal with CLECs such as Covad.

1. Verizon and Its *Amici* Try to Create a False Predatory Pricing Requirement for Section 2 Liability

As the Court put it in *Kodak*, what Verizon and its amici seek here would be "a radical departure in this Court's antitrust law." 504 U.S. at 479-80 n.29. They seek the creation of a new pleading rule, one that essentially imposes a predatory pricing requirement before a monopolist may be found to have engaged in an actionable refusal to deal. That proposed

amendment to the Sherman Act is both unfounded and ill-advised.

The United States argues that the Court should analyze claims against ILECs using the same "sort of analysis [it employs] with respect to predatory pricing." US/FTC Br. 16. That would be a massive change to, not an application of, the antitrust laws. It is true the courts "have recognized that conduct is exclusionary where it involves a sacrifice of short-term profits or goodwill that makes sense only insofar as it helps the defendant maintain or obtain monopoly power." *Id.* But that is not the *only* form of conduct that qualifies as exclusionary. Rather, the Section 2 jurisprudence of this Court and the lower courts recognizes that "the means of illicit exclusion, like the means of legitimate competition, are myriad." *Id.*, 14 (*quoting Microsoft*, 253 F.3d at 58).

That is why courts analyzing claims of exclusionary conduct have focused not on attempts to establish a list of practices that are (or are not) exclusionary, but have analyzed instead the "*anticompetitive effect*" of the challenged conduct. *Microsoft*, 253 F.3d at 58. Thus, conduct is exclusionary if it "harms the competitive process." *Town of Concord v. Boston Edison Co.*, 915 F.2d 17, 21 (1st Cir. 1990) (Breyer, J.). Contrary to Verizon's suggestion, *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585 (1985), did not require, to state a refusal to deal claim, that a monopolist forego profits or change a prior policy of dealing with competitors. To the contrary, *Aspen* recognized the broad and flexible nature of exclusionary conduct: "If a firm has been 'attempting to exclude rivals on some basis other than efficiency,' it is fair to characterize its behavior as predatory." 472 U.S. at 605 (*quoting* R. Bork, The Antitrust Paradox, 138 (1960)). *Aspen* went on to quote the Areeda and Turner definition of exclusionary conduct: "behavior that not only (1) tends to impair the opportunities of rivals, but also (2) either does not further competition on the merits or does so in an unnecessarily restrictive way." *Id.* at 605 n.32, (*quoting* P. Areeda & D. Turner, 3 *Antitrust Law* ¶ 626b, 78 (1978)). While the fact pattern in *Aspen* certainly

met that test, the Court has never – in *Aspen*, *Kodak* or elsewhere – pronounced that only forsaking profits would do so.[36]

2. Raising Rivals' Costs Is Exclusionary

Verizon's proposed test is obviously flawed because it exempts from liability any anticompetitive conduct that does not involve the sacrifice of profits. Among other things, it thus immunizes the well-recognized propensity of monopolists to destroy competition without ever foregoing a cent of profit, by raising their rivals' costs. *See generally* Thomas G. Krattenmaker & Steven C. Salop, *Anticompetitive Exclusion: Raising Rivals' Cost to Achieve Power Over Price*, 96 Yale L.J. 209, 224 (1986) ("Raising rivals' costs can be a particularly effective method of anticompetitive exclusion. This strategy need not entail sacrificing one's own profits in the short run. . . ."); *see also* Herbert Hovenkamp, *Post-Chicago Antitrust: A Review and Critique*, 2001 Colum. Bus. L. Rev. 257, 318-23 (2001) (discussing economic logic behind raising rivals' cost theory). Raising rivals' costs has been a primary mechanism by which ILECs have destroyed competition.

Where, as here, a monopolist controls inputs that are necessary to competition, it can thwart that competition by raising its rivals' costs of obtaining them. That may happen directly, as with the type of price squeeze condemned in the landmark *Alcoa* case, *United States v. Aluminum Co. of America*, 148 F.2d 416, 437-38 (2d Cir. 1945); *see also* Steven C. Salop, *Economic Concepts and Antitrust Analysis*, 56 Antitrust L.J. 57, 58-59 (1987) (evil of price squeeze is not predatory pricing; "rather, it is a claim that firms exclude rivals and gain power over price by raising their rivals' costs"). Monopolists have also found more subtle means to inflate their competitors' costs. *See, e.g.*, *Ball Mem'l Hosp., Inc. v. Mutual Hosp. Ins., Inc.*,

36. Indeed, the Seventh Circuit has interpreted *Aspen* to mean "a monopolist may be guilty of monopolization if it refuses to cooperate with a competitor in circumstances where some cooperation is indispensable to effective competition." *Olympia Equip. Leasing Co. v. Western Union Tel. Co.*, 797 F.2d 370, 379 (7th Cir.) (Posner, J.) *reh'g denied*, 802 F.2d 217 (1986), *cert. denied*, 480 U.S. 934 (1987). That is precisely what Respondent, and CLECs such as Covad, have alleged. The ILECs refuse to deal with CLECs with the specific knowledge that their refusal makes it impossible to compete.

784 F.2d 1325, 1339-40 (7th Cir. 1986) ("When a firm finds a way to confront its rivals with higher costs, it may raise its own prices to consumers without drawing increased output from them."); *Forsyth v. Humana, Inc.*, 114 F.3d 1467, 1478 (9th Cir. 1997), *aff'd*, 525 U.S. 299 (1999) (reversed summary judgment; policy raised factual question of whether conduct raised competitor's costs); *Multistate Legal Studies, Inc. v. Harcourt Brace Jovanovich Legal and Prof'l Publications, Inc.*, 63 F.3d 1540, 1553 n.12 (10th Cir. 1995) (raising rival's costs "would qualify as anticompetitive conduct unless [defendants] could demonstrate a legitimate business justification for it").

Verizon and its fellow ILECs have perpetrated both types of raising-rivals'-costs schemes – especially against facilities-based CLECs such as Covad. The ILECs have engaged in direct price squeezes, *see* p. 15, *ante*, and routinely employ countless mechanisms to make the interconnection process as time-consuming and costly as possible, *see* pp. 12-14, *ante*, all with no purpose but to extend their monopoly over the local telephone network into monopoly power over downstream markets such as the market for Internet access. The United States emphasized the exclusionary effects of just such a strategy, when used by AT&T:

> Even with respect to those limited facilities AT&T agreed to provide, it imposed a number of cumbersome and unnecessary technical and operational practices on its competitors which increased their costs and lowered the quality of their service, in marked contrast to the efficient interconnection arrangements made available to AT&T's own intercity private line connections.

Plaintiff's Memorandum in Opposition to Defendant's Motion for Involuntary Dismissal Under Rule 41(b), at 79, *United States v. AT&T Co.*, No. 74-1698 (D.D.C., filed Aug. 16, 1981). Yet the approach suggested by Verizon and the United States, which would require predatory pricing to state a refusal to deal claim, would place all that plainly anticompetitive conduct beyond the reach of the antitrust laws. That would indeed be a "radical departure" in the law.

The United States' position also appears to be a radical and unexplained departure from its prior position concerning CLEC antitrust claims against ILECs. The United States (together with the Federal Communications Commission) opined to the Court of Appeals for the Eleventh Circuit in 2001 that a CLEC's allegations of an ILEC's "failure to provide reasonable interconnection" under the 1996 Act - remarkably similar to the allegations asserted by Respondent here and by Covad in its lawsuits against ILECs - sufficiently "allege[d] exclusionary conduct by a firm with monopoly power that lacks business justification and that harms competition." *See* Brief for the United States and Federal Communications Commission as Amici Curiae in Support of Appellants, *Intermedia Comm., Inc. v. BellSouth Telecomm., Inc.*, No. 01-10224-JJ (11th Cir. filed Mar. 28, 2001) 25-26. Verizon and its amici offer no explanation how the antitrust laws have changed since then, so that such conduct is no longer exclusionary, as a matter of law.

3. ILECs Routinely Forego Profits to Harm Competition

Even if the Court adopted the new "predatory pricing" test proposed by Verizon and the United States, Verizon and its fellow ILECs would still be liable under it. Just as in *Aspen* and *Kodak*, to exclude their CLEC competitors, the ILECs *are* foregoing profits, by refusing to engage in what would otherwise be profitable sales. CLECs, after all, do not buy unbundled network elements from ILECs for free or even, as Verizon falsely suggests, at cost. Rather, the FCC has mandated that states price unbundled network elements using the Total Element Long Run Incremental Cost ("TELRIC") methodology, which expressly covers both the ILECs' costs and a reasonable profit. *Verizon*, 535 U.S. at 493, 500 n.19. Indeed, given that most elements of the local telephone network (including, notably, the many millions of essential local loops controlled by the ILECs) have been in place and funded by ratepayers for many decades, it is hard to imagine how the ILECs could claim the transactions are unprofitable.

CONCLUSION

For the foregoing reasons, the Court should affirm the judgment of court of appeals.

Respectfully submitted,

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